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IN THE

Supreme Court of the United States

October Term, 1969

No. 1543

IROQUOIS INDUSTRIES, INC.,
Petitioner,

v.

SYRACUSE CHINA CORPORATION, WILLIAM R. SALISBURY, FOSTER T. RHODES, MALCOLM E. KELLEY, JAMES SALISBURY PASS, ROBERT M. SALISBURY, HAROLD C. BROWN & CO., INC., HAROLD C. BROWN, C. HERBERT FEUCHTER, and TOWLE MANUFACTURING COMPANY,
Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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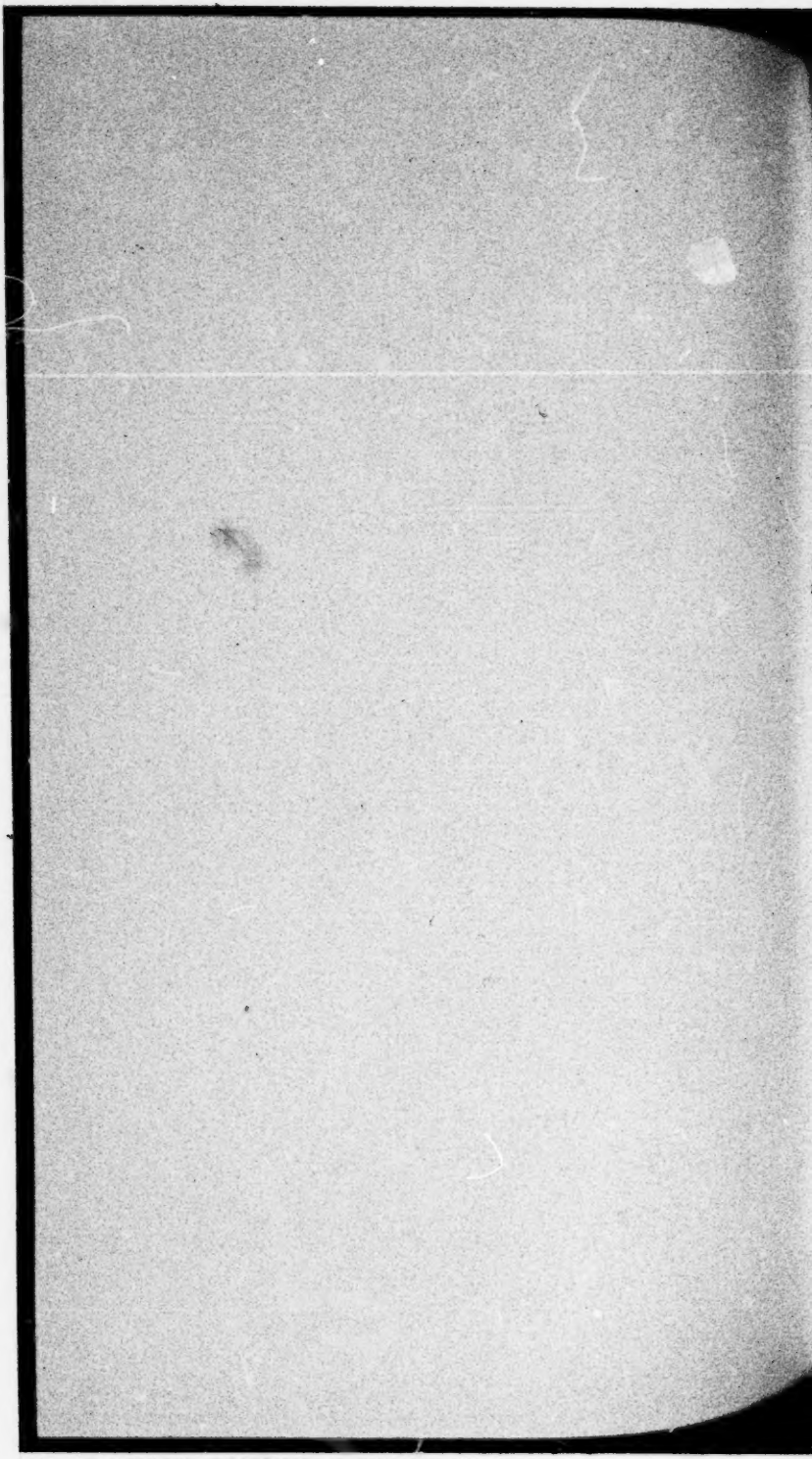

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Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Iroquois Industries, Inc., petitions for a writ of certiorari to review the order and judgment of the United States Court of Appeals for the Second Circuit that affirmed the dismissal on motion of the complaint on the grounds that it failed to state a claim upon which relief could be granted under Section 10(b) of the Securities Exchange Act of 1934, 15 U. S. C. § 78j(b) and Rule 10b-5 thereunder, 17 CFR § 240.10b-5.

OPINIONS BELOW

The opinion of the Court of Appeals (App. A, *infra*, pp. 29-42) is reported at 417 F. 2d 963 (2d Cir. 1969). The opinion of the District Court (App. B, *infra*, pp. 43-52) is reported at CCH Federal Securities Law Reporter, ¶ 92,301 (WDNY 1968).

JURISDICTION

The judgment of the Court of Appeals was entered on November 3, 1969. On December 10, 1969 the Court of Appeals, following the filing by the petitioner on November 17, 1969 of a timely petition for rehearing and rehearing *en banc*, denied such petition without opinion. On December 29, 1969 petitioner filed a motion in the Court of Appeals for leave to renew its petition for rehearing. The Court of Appeals granted such motion on February 11, 1970 and on the same day denied such renewed petition both without opinion. On February 6, 1970 Justice John M. Harlan extended until May 9, 1970 the time for the petitioner to file this petition. The jurisdiction of this court is invoked under 28 U. S. C. § 1254(1).

QUESTIONS PRESENTED

1. Must a plaintiff be an actual (as distinguished from an aborted) purchaser or seller of securities in order to have standing to assert a claim under Section 10(b) of the Securities Exchange Act of 1934, 15 U. S. C. § 78j(b) and Rule 10b-5 thereunder, 17 CFR § 240.10b-5.

2. In the event the plaintiff must be a purchaser or seller, does the complaint allege facts sufficient to show that the plaintiff falls within the "purchaser-seller" definition.

STATUTE AND RULE INVOLVED

Section 10(b) of the Securities Exchange Act of 1934, 15 U. S. C. § 78j(b) provides:

> SECTION 10. It shall be unlawful for any person, directly or indirectly, by the use of any means of instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—
>
> • • •
>
> (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

Rule 10b-5 of the Rules of the Securities and Exchange Commission, 17 CFR § 240.10b-5 provides:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,
>
> (1) to employ any device, scheme, or artifice to defraud,
>
> (2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,
>
> in connection with the purchase or sale of any security.

STATEMENT OF THE CASE

We set forth the statement from the opinion of the Court of Appeals (App. A, *infra*, pp. 31-32):

"Syracuse China is a New York corporation doing business in Syracuse. Syracuse China has outstanding 113,000 shares of common stock; there are some 600 stockholders. The individual defendants, except Brown and Feuchter, are officers or directors or both of Syracuse China. Defendant Harold C. Brown & Co., Inc. (Brown Inc.) is an investment banking house in Buffalo. The individual defendants Brown and Feuchter are connected with Brown Inc. Defendant Towle is a Massachusetts corporation which also does business in New York City.

"Iroquois invited stockholders of Syracuse China to tender their shares for purchase and Iroquois agreed to purchase all shares tendered, up to 50,000 shares.

"The defendants conspired together to prevent Iroquois from obtaining shares under the tender offer and *did prevent* Iroquois from obtaining shares. The defendants retained professional solicitors, at the expense of Syracuse China, who persuaded stockholders not to tender their shares. The defendants themselves asked stockholders not to tender. Letters were written by defendants to the stockholders, *falsely stating* that Syracuse China was negotiating a merger, that negotiations for a merger with Towle were continuing, and that details of the merger would shortly be submitted; in fact, *there was never any intention to conclude any merger with Towle* but the talk was to *mislead* and to interfere with the tender offer. The *letters of Syracuse China were false and misleading.* The defendants advised stockholders that members of manage-

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ment would buy their shares if any stockholder wanted to sell; in fact, members of management did purchase a substantial number of shares. *Towle aided the other defendants by conducting sham merger negotiations, knowing that no merger was intended.* Brown Inc. and its officers and employees refused to advise the customers of Brown Inc. of the tender offer of Iroquois but instead advised them to sell their shares to members of the management of Syracuse China." (Italics ours.)

The United States District Court for the Western District of New York whose jurisdiction was invoked under Section 27 of the Securities Exchange Act of 1934, 15 U. S. C. § 78aa, granted the defendants' motions to dismiss the complaint under F. R. C. R. 12(b)(6) for failure to state a claim upon which relief can be granted. The Court of Appeals affirmed this decision on the grounds "that a civil action under Section 10(b) of the 1934 Act (15 U. S. C. § 78j(b)) may be maintained only by a purchaser or seller of securities." (App. A, *infra*, p. 30)

While recognizing "that liability under Rule 10b-5 does not depend on a securities transaction between plaintiff and defendant" (App. A, *infra*, p. 36) and "that there need not be 'privity' between plaintiff and defendant" (App. A, *infra*, p. 36) and the "cited statute and Rule make it unlawful to employ fraud 'in connection with the purchase or sale of any security' " (App. A, *infra*, p. 32), the Court of Appeals nevertheless held that the plaintiff Iroquois lacked standing to assert a claim under the section and rule because it was not an actual purchaser.

Thus, the Court of Appeals held that although the statute and rule were violated by the defendants and the plaintiff

was prevented from purchasing shares as a result thereof, plaintiff lacked standing to assert its claim. This holding of lack of standing was erroneously thought to follow from the court's premise that the statute and rule require the plaintiff to be either an actual purchaser or seller. In so finding, the court relied principally on its 17 year old holding in *Birnbaum v. Newport Steel Corp.*, 193 F. 2d 461 (2d Cir. 1952), *cert. denied*, 343 U. S. 956 (1952) and distinguished the two cases[1] in the Second Circuit that seemed to indicate that the purchaser-seller limitation had been abandoned or at least relaxed. The court rejected the claim of the petitioner and the Securities and Exchange Commission (appearing as *amicus curiae* in support of the plaintiff) that neither the history of, nor the statute and rule themselves, require the purchaser-seller limitation. The Court of Appeals ignored the fact that Iroquois received tenders for and actually purchased 9,000 shares. It invited tenders for 50,000 shares (complaint, para. 21) and it was deprived of 41,000 shares (complaint, para. 29). It sought injunctive relief as well as damages (complaint, *ad damnum* clause). Thus, even in the strictest view of the purchaser-seller test Iroquois should be held to have standing.[2]

However, having formulated the purchaser-seller test and having recited the facts ignoring Iroquois' actual purchase, and also ignoring the fact that the trial court could

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[1] *Vine v. Beneficial Finance Co.*, 374 F. 2d 627 (2d Cir. 1967) *cert. denied*, 389 U. S. 970 (1967) and *A. T. Brod & Co. v. Perlow*, 375 F. 2d 393 (2d Cir. 1967).

[2] Even the Second Circuit recognizes that the purchaser-seller limitation does not apply where an injunction rather than damages is sought. *Mutual Shares Corp. v. Genesco*, 384 F. 2d 540 (2d Cir. 1967); see also, App. A, *infra*, p. 37.

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fashion legal or equitable relief,[3] the Court of Appeals affirmed the dismissal of the complaint.

REASONS FOR GRANTING THE WRIT

The ruling below bars any remedy for an undisputed violation of federal law and is in conflict with decisions of this court declaring that the congressional purpose must be made effective by providing a remedy when a violation occurs. The decision of the Second Circuit is in conflict with decisions of other Circuits. The principle announced by the lower court would apply, if unreversed, to a broad range of cases arising under the securities laws requiring full and honest dissemination of information regarding securities. It narrows the broad remedial federal policy to overly restrictive limits. It creates unnecessary obstacles to effective relief and to private enforcement of federal commands on which Congress relied for effective law enforcement. Importance is measured not merely by the distortion of congressional policy, but by impairment of shareholder and public interests which the Securities Exchange Act was enacted to protect.

1. Decisions of the Circuit Courts that have passed upon the question are in conflict.

The holding of the court below[4] that in order to have standing under Section 10(b) of the 1934 Act and under Rule 10b-5 a claimant must be an actual purchaser or seller, directly conflicts with the decision of the Court of Appeals for the Third Circuit in *Kahan v. Rosenstiel*, ___ F. 2d ___, CCH Fed. Sec. L. Rep. ¶ 92,589 (3d Cir. Feb. 20, 1970). There the court stated:

---

[3] *J. I. Case v. Borak*, 377 U. S. 426 (1964).

[4] This Court has not heretofore passed on the question of "standing" in the context presented by this case. See, *SEC v. National Securities*, 393 U. S. 453, 467, fn. 9 (1969)

> "The present case represents the first time this Circuit has addressed itself to the question whether Section 10(b) may be enforced by a private party who is neither a purchaser nor seller. **The Circuits which have decided the issue are divided.** The Seventh and Eighth Circuits require that plaintiffs be purchasers or sellers even where injunctive relief is sought. *Greater Iowa Corporation v. McLendon*, 378 F. 2d 783 (8th Cir. 1967) (following Birnbaum); *Jachemec v. Schenley Industries, Inc.*, No. 15024 (7th Cir. 1965) *cert. denied*, 382 U. S. 841 (1965). The Second Circuit has construed the statute more broadly at least where an injunction is sought. The Sixth Circuit has also indicated that in a suit for injunctive relief the requirements may be liberalized. In *Britt v. The Cyril Bath Co.*, 417 F. 2d 433, 436 (6th Cir. 1969), that court stated that in a suit under § 10(b), the necessary causal connection between the fraud alleged and the resultant purchase or sale of a security might be relaxed" (emphasis ours).

To the list of Circuits referred to in the above quotation that have considered the "purchaser-seller" limitation should be added the Fifth and Ninth. On the strength of *Iroquois* the Fifth Circuit adhered to the limitation in *Rekant v. Desser*, CCH Fed. Sec. L. Rep. ¶___, ___ F. 2d ___, Docket No. 25872, Slip Opinion, pp. 10-11 (5th Cir. Apr. 20, 1970) stating:

> "*Birnbaum* has been shot at by expert marksmen. The buyer-seller requirement for standing has been criticized as too strict a reading of the rule . . . Bloody but unbowed *Birnbaum* still stands."

The holding of the court below also directly conflicts with the decision of the Court of Appeals for the Ninth Circuit in *Errion v. Connell*, 236 F. 2d 447 (9th Cir. 1956). There an eighty year old widow was induced to sell securities and to use the proceeds and other securities to purchase worthless tidelands represented to be oyster beds worth $1,200 per acre. The court held, 236 F. 2d at 454:

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> "We are of the opinion that the Act of 1934 was designed to cut out 'sharp practices' and fraudulent schemes *involving* securities, and the fact that there may be a co-mingling of securities with non-securities in the scheme does not oust the United States District Court of jurisdiction." (Italics ours.)

This court should resolve the conflict because it involves an important issue which directly affects the administration of the securities law both through private civil actions and through Commission enforcement.

2. The history of the rule and its interpretation by the Securities and Exchange Commission indicate that there is no purchaser-seller limitation contained therein.

The basis assigned by the court below for the purchaser-seller limitation is the Commission's statement of intentions upon the issuance of Rule 10b-5 in May, 1942 (App. A, *infra*, p. 33). No purchaser-seller limitation is found in the language of Section 10(b) or in the language of the rule. That the Commission has no present intention of thus limiting the scope of Rule 10b-5, and probably had no such intention at the time of its issuance, is amply demonstrated by the various *amicus* briefs and other formal and informal statements emanating from the Commission. For example, in *Vine v. Beneficial Finance Co.*, 374 F. 2d 627, 636 (2d Cir. 1967), *cert. denied*, 389 U. S. 970 (1967) the court expanded the definition of a seller and found it "unnecessary" to consider the "interesting contention" of the Commission that a plaintiff in a Section 10(b) action need not be either a purchaser or a seller.

Again, in *A. T. Brod & Co. v. Perlow*, 375 F. 2d 393, 397 (2d Cir. 1967) the court noted that criticism by the Commission of the interpretation in *Birnbaum* as "too

narrow" would not be considered because the plaintiff "is clearly a purchaser of securities."

That the Commission still adheres to its view is borne out by the fact that it filed a brief as *amicus curiae* in support of the petitioner's position in the Court of Appeals and stated at pp. 20-22 thereof (footnotes omitted):

> "It is the Commission's view that standing to seek damages under Rule 10b-5 should not be governed by any mechanical rule requiring the plaintiff to be a purchaser or seller. The proper test should be whether the plaintiff is within the class of persons intended to be protected by the statute against the harm caused by the defendant's violation. 'In determining who has standing to enforce duties created by statute, a court's quest must be for what will best accomplish the purposes of the legislature.' *Electronic Specialty Co. v. International Controls Corp.*, Docket Nos. 33073/4/5 and 33105, slip opinion p. 1104 (C. A. 2, Jan. 24, 1969). [409 F. 2d 937, 946] The Securities Exchange Act was intended to insure the maintenance of fair and honest securities markets, and accordingly those who participate in such markets are entitled to the Act's protections. This means that, subject to such limitations as may be appropriate in particular situations, persons whose investment decisions are influenced by misrepresentations made in violation of the Act should have standing to sue for damages caused by the violation. This category of protected persons includes not only those who are deceived into making purchases and sales; it may also include those who are deceived into holding securities which they already own, at least when the misrepresentations are made for the purpose of inducing such persons to hold their securities. We believe that this result necessarily follows from the conclusion reached in Part A of this brief, supported by the *Texas Gulf Sulphur* decision, that Rule 10b-5 is applicable to all misrepresentations which are likely to influence investors' decisions to buy, sell or hold securities.
>
> "The availability of the Act's protections, however, is not limited to persons who are themselves deceived.

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> Participants in the securities markets are entitled to expect that the Act will provide them an honest market place in which to do business. Thus, it is not enough that a person entering the market have protection against being himself deceived. He also needs and expects protection against injury which he will necessarily suffer, in connection with his transactions and proposed transactions in securities, as a result of deception practiced upon others; if, as the complaint alleges here, deception is practiced upon others for the purpose of preventing *him* from entering into securities transactions with these other persons, and he is so prevented, he should be entitled to sue for resulting damages. The Supreme Court has pointed out that private rights of action are 'a necessary supplement' to the Commission's own enforcement activities. *J. I. Case Co. v. Borak*, 377 U. S. 426, 432 (1964). To deny relief to a person in Iroquois' position would defeat his reasonable expectations concerning the securities markets and would be inconsistent with the statutory purpose."

The House Report on the Securities Exchange Act emphasized that the 1934 Act was intended to insure "straight shooting" in securities transactions.[5] It should be noted, however, that the words "purchase" and "sale" are sufficient on their face, even before consideration is given to the statutory purpose, to encompass the situation with which we are here concerned. In view of the principle that the Act should be interpreted broadly, it seems reasonable to construe the words "purchase" and "sale" to include those steps which are necessary or appropriate in bringing about a purchase or sale transaction—such as offers, proposals and attempts to buy or sell—even though the transaction itself is never consummated. Defendants' alleged misrepresentations in the instant case are clearly covered by this construction; they were made in an effort

[5] H. R. Rep. No. 1383, 73d Cong., 2d Sess. 5 (1934).

to induce the Syracuse shareholders not to sell their stock and thus were likely to thwart the tender offer through which Iroquois proposed and attempted to acquire that stock.

This construction of "purchase" and "sale" is reinforced by the statutory purpose. The Act, as its title declares, was designed "[t]o provide for the regulation of securities exchanges and of over-the-counter markets . . . [and] to prevent inequitable and unfair practices on such exchanges and markets . . ." 48 Stat. 881. Congress intended, as stated in Section 2 of the Act, 15 U. S. C. 78b, "to provide for regulation and control" of "transactions in securities as commonly conducted upon securities exchanges and over-the-counter markets" and also of "practices and matters related thereto." and "to impose requirements necessary to make such regulation and control reasonably complete and effective," in order "to insure the maintenance of fair and honest markets in such transactions." It has been pointed out that the Act was designed "to keep the channels of interstate commerce, the mail, and national security exchanges pure from fraudulent schemes, tricks, devices, and all forms of manipulation." *Hooper v. Mountain States Sec. Corp.*, 282 F. 2d 195, 202 (5th Cir. 1960), *cert. denied*, 365 U. S. 814 (1961).

In this connection it is clear that the plaintiff is a reliable private attorney general to litigate the issues in the public interest in the present case. In *Data Processing Service v. Camp*, ___ U. S. ___, 25 L. Ed. 2d 184, 188 (1970) this court held:

> "The 'legal interest' test . . . concerns . . . the question whether the interest sought to be protected by the complainant is arguably within the zone of interests to be protected or regulated by the statute or

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> constitutional guarantee in question. . . . Certainly he who is 'likely to be financially injured, . . . may be a reliable private attorney general to litigate the issues of the public interest. . . .'"

The decision below stifles private enforcement suits, a necessary supplement to Commission action in enforcing the Act, by raising insuperable obstacles to relief. This "necessary supplement" is virtually destroyed as an "effective weapon" by the holding below. The individual shareholders of Syracuse China are not in a position to bring an action as suggested by the District Court (App. B, *infra,* p. 50). They are the "little investors who need the greatest possible protection." *Surowitz v. Hilton Hotels Corp.,* 383 U. S. 363, 371 (1966). Yet the court below would relegate the cause of action to the small shareholder to litigate. No small investor could afford to rebut the array of expert witnesses produced by the corporation by himself engaging expert witnesses, causing exhaustive audits and investigations of the books and records of huge corporations, by the taking of lengthy depositions and by financing such items as the court reporting of a protracted trial. If the time, expense and staff requirements of such an undertaking are not available to the Commission (*J. I. Case v. Borak,* 377 U. S. 426, 432 (1964)), obviously the small investor, whose total stake may be less than such costs is never in a position to undertake a full-dress trial.

This court recognized the danger of chilling private actions when it said in *J. I. Case v. Borak* (377 U. S. at 435):

> ". . . the hurdles that the victim might face (such as separate suits . . . security for expense statutes, bringing in all parties for complete relief, etc.) might well prove insuperable to effective relief."

The history, policy and construction of the statute and rule leads to the inescapable conclusion that neither Con-

gress nor the Commission intended that the plaintiff must be either a purchaser or seller in order to assert a claim under Section 10(b) or Rule 10b-5.

3. Artificial modification and relaxation of the purchaser-seller requirement by expanding the definition of purchaser and seller is no substitute for elimination of the rule.

As noted above, the numerous modifications to the Birnbaum purchaser-seller limitation since its adoption have led the Commission to conclude that the doctrine has been "eroded" and "weakened" and many commentators to write about the "demise" of the doctrine.[6]

The modifications that have caused this divergence of view fall into several broad categories—the "involuntary seller," the aborted transaction, protection for non-investors, and equitable relief. Some cases suggest that the plaintiff has standing under Rule 10b-5 only when the purchase or sale transaction has been completed, while others provide standing even though a purchase or sale has not been consummated.

Forced Sellers. The "involuntary seller" rule is based primarily upon *Vine v. Beneficial Finance Co.*, 374 F. 2d 627 (2d Cir. 1967), *cert. denied* 389 U. S. 970 (1967), in which a plaintiff who did not tender his stock to an offeror alleged that the latter, acting in concert with the corporate officers, acquired shares for an inadequate consideration. Following the successful tender offer, the defendants completed a short-form merger of the corporation.

[6] See, *i.e.*, Lowenfels, The Demise of the Birnbaum Doctrine: A New Era for Rule 10b-5. 54 Va. L. Rev. 268 (1968).

Although the plaintiff did not actually sell his stock, the court held that, since he was faced with a choice between converting his stock into a claim for cash or retaining his stock in a non-existent corporation, he was an "involuntary seller," and therefore within the *Birnbaum* rule.

Aborted Transactions.[7] Among the decisions that recognize plaintiff's standing even in the face of an aborted securities transaction is *Opper v. Hancock Securities Corp.*, 367 F. 2d 157 (2d Cir. 1966), in which the court, without discussion, upheld a judgment awarding damages to a plaintiff who was not a purchaser or seller with respect to the defendant's fraud. Plaintiff was an investor who had ordered his broker to sell his stock, but, because of the broker's fraudulent decision to sell his own securities instead, the sale was not consummated. Similarly, in *Goodman v. H. Hentz & Co.*, 265 F. Supp. 440, 444 (ND Ill. 1967), the court rejected a contention stating that "plaintiffs were actual parties to transactions which, [but] for the fraud of [defendant], would have been actual purchases or sales of securities by the plaintiff." In *Stockwell v. Reynolds & Co.*, 252 F. Supp. 215, 219 (SD NY 1965), it was held that "a seller is injured as much when he suffers a loss on the sale of securities which he has been fraudulently induced to retain as when he is fraudulently induced to sell them."

Non-Investors. The decision in *A. T. Brod & Co. v. Perlow*, 375 F. 2d 393 (2d Cir. 1967), has sometimes been construed as another case involving an aborted sale, although it appears to be more significant as a decision that recognizes Rule 10b-5 to be applicable to others than investors. In that case, a broker sought monetary damages to com-

[7] As a minimum the petitioner should be placed in this exception to the purchaser-seller limitation.

pensate him for his customer's fraudulent failure to pay for securities he had ordered. Although some have regarded the broker as an aborted seller, because of his customer's failure to buy, the court indicates in a footnote, 375 F. 2d at 397, that it regarded the broker as a purchaser of securities. Other non-investors who have been given standing under Rule 10b-5 include issuing corporations,—*e.g.*, the status of an issuing corporation as a "seller" of its securities was recognized in *Hooper v. Mountain Securities Corp.*, 282 F. 2d 195 (5th Cir. 1960), in which a corporation's trustee in bankruptcy was allowed to maintain an action on behalf of the corporation, which was allegedly misled by fraud into issuing stock for worthless assets. In *Ruckle v. Roto American Corp.*, 339 F. 2d 24 (2d Cir. 1964), a similar result was reached in a derivative action brought to restrain the defendant directors from consummating a fraudulent plan to issue additional shares of treasury stock to one of the directors. In this case, standing was recognized even though the "sale"—that is, the issuance of the securities—had not yet taken place. Indeed, in *A. T. Brod & Co. v. Perlow*, 375 F. 2d 393, 397 (2d Cir. 1967), the court held:

> "We believe that § 10(b) and Rule 10b-5 prohibit *all* fraudulent schemes in connection with the purchase or sale of securities, whether the artifices employed involve a garden type variety of fraud, or present a unique form of deception. Novel or atypical methods should not provide immunity from the securities laws."

Injunctive Relief. Relaxation of the *Birnbaum* doctrine in cases of equitable relief is exemplified by *Mutual Shares Corp. v. Genesco, Inc.*, 384 F. 2d 540, 547 (2d Cir. 1967), in which plaintiffs who were not shareholders at the time of the alleged fraudulent transactions were denied standing to maintain their action for monetary damages, but were

granted equitable relief because of the continuing nature of the manipulative scheme. The basis of the decision is that stockholders who continue to hold their stock are, like the SEC, "logical plaintiffs" to play an important role in enforcement of the Act, even though their claim for damages "founders both on proof of loss and the causal connection with the alleged violation of the Rule."

In *Crane Co. v. Westinghouse Air Brake Co.*, 419 F. 2d 787 (2d Cir. 1969), decided only five weeks after *Iroquois*, the alleged misrepresentations that defeated Crane's tender offer emanated not from the target company's management but from one of the tender offeror's major competitors in the plumbing industry, American Standard, which subsequently effected a merger with the target corporation. Because of Standard's substantial holdings in the target corporation, coupled with its close cooperation with the target company's management, it was held to be an insider, and its market manipulations to raise the price of the target company's stock, so as to make the tender offer unattractive, were held to be a violation of Rule 10b-5. Crane's standing under the *Birnbaum* doctrine was held to come within the "involuntary seller" rule of the *Vine* decision, since the antitrust laws would force Crane to divest itself of stock it had acquired in a corporation now merged with one of its major competitors.

It seems clear that the Second Circuit has gone beyond *Vine* in its decision in *Crane*. In *Vine* the stockholders by operation of law were forced to either exchange their shares or to convert them. In the *Crane* case, Crane was not forced by operation of law into selling its shares of Air Brake stock. For example, Crane has the choice of contesting any antitrust suit brought by Standard, if in fact Standard actually chose to bring such a suit.

Albeit decided by different panels, it is interesting and important to note that the Second Circuit held in *Crane* unlike its holding in *Iroquois* that an aborted seller has the requisite standing as the court stated (419 F. 2d at 796):

> "When securities are subject to trading dominated by an insider such as Standard, there is an obligation to disclose material information to the investing public, and this duty gives rise to liability under 10b-5 to *third persons* who, as a result of the deception practiced upon the public, are *prevented* from entering into securities transactions with members of the public. When Crane entered the securities market with its tender offer, it was entitled to the Act's protection not only against being deceived itself but also against deception of the investing public designed to prevent the public from entering into securities transactions." (Italics added)

The decision in *Crane* also raises interesting questions. If the defrauding manipulator had been anyone other than Standard—any one of thousands of companies or millions of investors—would the identical circumstances have left Crane without standing, inasmuch as there would have been no antitrust requirement of divestiture? Is the protection of Section 10(b) properly grounded on such fortuitous circumstances? Furthermore, if Standard's manipulations had been *totally* effective, and had prevented Crane from acquiring *any* shares pursuant to its tender offer, would not Crane be barred from maintaining its action because it had no shares that the antitrust laws required it to sell? Apparently, if a thing is worth doing—even fraud—it is worth doing well.

The authorities uniformly have rejected a formalistic and superficial approach to the application and interpretation of federal statutes. This court in *Electric Bond & Share Co. v. Securities & Exchange Commission*, 303 U. S.

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419, 440 (1938), appositely rejected the use of formalistic devices in attempts to escape proscriptions or applications of federal statutes:

> "It is the substance of what they do, and not the form in which they clothe their transactions, which must afford the test. The constitutional authority confided to Congress could not be maintained if it were deemed to depend upon the mere modal arrangements of those seeking to escape its exercise. Compare *Northern Securities Co. v. United States*, 193 U. S. 197."

The defendants have perpetrated one of the great evils that Congress sought to eliminate. It should be remembered "that statutes always have some purpose or object to accomplish, whose sympathetic and imaginative discovery is the surest guide to their meaning." *Cabell v. Markham*, 148 F. 2d 737, 739 (2d Cir. 1945), *aff'd* 326 U. S. 404 (1945). It is clear that the federal courts have the power to fashion whatever remedy is appropriate in order to make the federal securities acts effective. *Deckert v. Independent Shares Corp.*, 311 U. S. 282 (1940); *J. I. Case Co. v. Borak*, 377 U. S. 426 (1964).

Returning to our starting point, the Commission is quite accurate in its conclusion that the purchaser—seller doctrine has been eroded and weakened, if not eliminated. Modification and relaxation of the rule and artificial definitions of purchaser and seller serve no useful purpose and only thwart the prophylactic affect of private rights to enforce the securities acts. To leave *Birnbaum* and *Iroquois* standing would be to leave scarecrows in the law. A reversal of *Iroquois* would serve a salutary and important public purpose.

4. There is no logical or legal reason why the purchaser-seller limitation should not apply when equitable relief is sought and why such limitation should apply when damages are sought.

The broad sweep of Section 10(b) and Rule 10b-5 make it unlawful for *any* person to employ *any* fraudulent device upon *any* person in connection with the purchase or sale of *any* security. We find no limiting language stating that the command of the statute and the rule shall apply in situations where equitable relief is sought but not in situations where damages alone are sought. We cannot conceive of any public policy that should so limit the congressional purpose in adopting the statute and authorizing the Commission to implement it.

There is no justification to be found in the legislative history of the Act or in the cases for reading Rule 10b-5 as if it read merely "in the purchase or sale" rather than "*in connection with* the purchase or sale." *Goodman v. H. Hentz and Co.*, 265 F. Supp. 440, 444 (ND Ill. 1967).

Although defendants' purpose may have been only to induce the shareholders not to sell their Syracuse stock, the alleged misrepresentations were also likely to induce them to make purchases of such stock. This likelihood of inducing purchases was sufficient in itself, regardless of what defendants' purpose may have been, to satisfy the requirement in Section 10(b) and Rule 10b-5 that the misrepresentations be "in connection with the purchase or sale of any security." *Heit v. Weitzen*, 402 F. 2d 909, 913 (2d Cir. 1968). As stated in *Securities & Exchange Commission v. Texas Gulf Sulphur Co.*, 401 F. 2d 833, 860, 861 (2d Cir. 1968) (footnote omitted, emphasis added):

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". . . Congress when it used the phrase 'in connection with the purchase or sale of any security' intended only that the device employed, whatever it might be, be of a sort that would cause reasonable investors to rely thereon, and, in connection therewith, so relying, cause them to purchase or sell a corporation's securities . . ."

* * *

". . . [T]he investing public is hurt by exposure to false or deceptive statements *irrespective of the purpose underlying their issuance.*"

Moreover, even if it be assumed that there was no likelihood that defendants' alleged misrepresentations would cause investors to make purchases, Rule 10b-5 was still violated, since the requirement that the misrepresentations be "in connection with the purchase or sale of any security" is satisfied also by misrepresentations which may be likely only to cause investors to refrain from entering into securities transactions. This principle was recognized in *Stockwell v. Reynolds & Co.*, 252 F. Supp. 215 (S. D. N. Y. 1965), which held that Rule 10b-5 was violated where misrepresentations induced persons not to sell securities. This principle is also implicit in the definiton of "materiality" set forth in the *Texas Gulf Sulphur* case, where the court stated that material facts include "those which may affect the desire of investors to buy, sell, or *hold* the company's securities," 401 F. 2d at 849 (emphasis added), and was further recognized by the court in its conclusion in that case that misrepresentations are made "in connection with the purchase or sale of . . . [a] security" if they are made "in a manner reasonably calculated to influence the investing public . . ." 401 F. 2d at 862.

The "in connection with" phrase, including the terms "purchase" and "sale," is part of a statute which is to

"be construed like other securities legislation 'enacted for the purpose of avoiding frauds,' not technically and restrictively, but flexibly to effectuate its remedial purposes." *Securities & Exchange Commission v. Capital Gains Research Bureau, Inc.*, 375 U. S. 180, 195 (1963); *see Tcherepnin v. Knight*, 389 U. S. 332, 336 (1967); *Stockwell v. Reynolds & Co.*, 252 F. Supp. 215, 219 (S. D. N. Y. 1965). In the recent decision of this court in *Securities & Exchange Commission v. National Securities, Inc.*, 393 U. S. 453, 466-467 (1969), after pointing out that "Section 10(b) and Rule 10b-5 together constitute one of the several broad antifraud provisions contained in the securities laws" and that, "[f]or the statute and the rule to apply, the allegedly proscribed conduct must have been 'in connection with the purchase or sale of any security,'" the court noted that "[t]he relevant definitional sections of the . . . Act . . . declare generally that the terms 'purchase' and 'sale' shall include contracts to purchase or sell."[8] This court stated that these definitions

> "indicate the breadth of the statutory terms by using the definitional word 'include' and by including within the definitions contracts 'to buy, purchase or otherwise acquire' and 'to sell or otherwise dispose of' securities."[9]

We should not lose sight of the fact that Iroquois by the fraud of the defendants was deprived of 41,000 shares

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[8] The terms "purchase" and "sale" are defined in Section 3(a)(13) and 3(a)(14), 15 U. S. C. 78c(a)(13) and 78c(a)(14), as follows:

Section 3. (a) When used in this title, unless the context otherwise requires—

* * *

(13) The terms "buy" and "purchase" each include any contract to buy, purchase or otherwise acquire.

(14) The terms "sale" and "sell" each include any contract to sell or otherwise dispose of.

[9] See also *Vine v. Beneficial Finance Co.*, 374 F. 2d 627, 634 (2d Cir. 1967), *cert. denied*, 389 U. S. 970 (1967), a suit under Rule 10b-5, where the court stated that "it has been pointed out that the verb 'include,' rather than the verb 'means,' emphasizes the breadth" of this definition.

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and that it in fact purchased 9,000 shares. Consequently, even under the purchaser-seller limitation Iroquois was a purchaser, and with respect to the 41,000 shares Iroquois was an aborted purchaser. With respect to the 41,000 shares that Iroquois failed to obtain because of the defendants' deception, the damages are direct. Another element of damages is the damages respecting the 9,900 shares that were acquired. But for the wrong perpetrated by the defendants, these 9,000 shares would have been part of a "control block" and accordingly would have taken on additional value. The court held in *Crane Co. v. Westinghouse Air Brake Co.*, 419 F. 2d 787, 798 (2d Cir. 1969):

> "The purchase-sale requirement must be interpreted so that the broad design of the Exchange Act, to prevent inequitable and unfair practices on securities exchanges and over-the-counter markets, is not frustrated by the use of novel or atypical transactions."

It is important to note that the court in *Crane*, after stating that the "purpose of Congress in enacting section 9(a)(2) and 10(b) was to protect the investing public from manipulation and deception by the use of devices which defrauded or misled investors in securities transactions" stated in footnote 14:

> "Congress when it used the phrase 'in connection with the purchase or sale of any security' *intended only that the device employed*, whatever it might be, be of a sort that would cause reasonable investors to rely thereon, and, in connection therewith, so relying, cause them to purchase or sell a corporation's securities." (Italics ours) (419 F. 2d at 798).

Thus, after deciding Iroquois even the Second Circuit realized that the "in connection with" phrase referred only to the device used and was not to a limitation on the standing of the injured party.

That there is no meaningful distinction between equitable relief and damages at law in determining the standing of a claimant is highlighted by the Third Circuit's decision in *Kahan v. Rosenstiel*, ____ F. 2d ____, CCH Fed. Sec. L. Rep. ¶ 92,589 (3d Cir. Feb. 20, 1970) where the impact of the purchaser—seller limitation announced in *Birnbaum* and *Iroquois* was avoided by resorting to the omnibus prayer for relief and holding that because equitable relief although not specifically requested could be granted under such circumstances the plaintiff had the requisite standing. The case at bar is even more compelling because the plaintiff in the *ad damnum* clause has specifically requested injunctive relief as well as "such other and further relief as to the court may seem just and proper." In *Kahan v. Rosenstiel, supra*, the Third Circuit held:

> "Defendants contend that even if a more liberal interpretation of the statute is appropriate for injunctive relief the plaintiff here failed to request such relief and hence the complaint may not be so construed. Plaintiff's complaint does not specifically ask for equitable relief; it contains only the general request for 'further relief as may be just.' Nonetheless, under Rule 54(c) of the Federal Rules of Civil Procedure, a court may have awarded any relief indicated under the circumstances. See *United States v. Maryland Casualty Company*, 384 F. 2d 303, 304 (2d Cir. 1967); *Arley v. United Pacific Insurance Company*, 379 F. 2d 183, 187 (9th Cir. 1969); *Whittaker v. Wall*, 226 F. 2d 868, 872 (8th Cir. 1955); *Fanchon & Marco, Inc. v. Paramount Pictures Inc.*, 202 F. 2d 731, 734 (2d Cir. 1953). Plaintiff's 10(b) suit would not have been dismissed even though the complaint did not request injunctive relief, if a cause of action for injunctive relief were in fact inherent in the complaint.
>
> "Plaintiff has set forth sufficient allegations of misrepresentations, manipulations and nondisclosures of

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material facts 'in connection with the sale or purchase of securities' so as to entitle him to the opportunity to proving a violation of the Act. If the allegations of the complaint are taken in the light strongest for the plaintiff, as we are obligated to do on a motion to dismiss, then it is conceivable that plaintiff's pleading has alleged such misconduct by the defendants."

It is difficult, if not impossible, to distinguish between one who makes a purchase based upon another's fraud and one who is unable to make a puchase based upon another's fraud. The damages in both cases are the same. The relief afforded by the statute and the rule, therefore, should be the same. It is equally difficult to distinguish between one who is unable to make a purchase based upon another's fraud and seeks injunctive relief and one who is unable to make a purchase based upon the same fraud and seeks damages. Had the petitioner been aware of the deception being practiced by the defendants while the tender offer was open it could have sought an injunction, but because the discovery was made later it should not lose its standing and therefore its claim. This would be a windfall for the defendants. The choice of remedies should be open and the standing should be the same in each instance.

Congress charged the courts to "be alert to provide such remedies as are necessary to make effective the congressional purpose" (*Borak*, 377 U. S. at 433, 434) in *all* cases, not only where equitable relief is sought. "[T]here is no reason to emasculate the securities laws by forbidding remedies which might prove to be essential." *Securities & Exchange Commission v. National Securities, Inc.*, 393 U. S. 453, 463 (1969).

5. The recent tender offer legislation does not render unimportant for the future the questions involving Rule 10b-5 presented by this case.

Amendments to the Securities Exchange Act imposing certain requirements with respect to tender offers were enacted on July 29, 1968, shortly before the decision in this case by the district court but subsequent to the events charged in the complaint. Sections 14(d), (e) and (f) of the Act, 15 U. S. C. A. 78n(d), (e) and (f). The enactment of these amendments, however, did not indicate that Section 10(b) and Rule 10b-5 were previously inapplicable to tender offers, nor did it render unimportant for the future the questions involving Rule 10b-5 presented in this case.

Section 14(e) of the Act, as added by the tender offer amendments, is an antifraud provision similar to Section 10(b) and Rule 10b-5 but expressly applicable to tender offers. This provision was enacted not because Section 10(b) and Rule 10b-5 were considered inapplicable to tenders offers, but rather out of an abundance of caution. In *Electronic Specialty Co. v. International Controls Corp.*, 409 F. 2d 937, 940 (2d Cir. 1969) the court held:

> "In effect [Section 14(e)] applies Rule 10b-5 both to the offeror and to the opposition—*very likely*, except *perhaps* for any bearing it may have on the issue of standing, only a codification of existing case law" (italics ours).

Thus, even on the question of standing, the Second Circuit recognized that only "perhaps" did Section 14(e) add anything to Rule 10b-5. While standing to sue may be broader under Section 14(e) than under Rule 10b-5 in certain areas, such as suits by the target corporation, the statutory purpose requires that Rule 10b-5 afford standing to a plaintiff in the position of Iroquois. That the same

conduct may violate both Rule 10b-5 and Section 14(e) is of no moment. As this court pointed out with respect to a similar situation—the overlap between Rule 10b-5 and the proxy rules adopted under Section 14(a) of the Act—"[t]he fact that there may well be some overlap is neither unusual nor unfortunate." *Securities & Exchange Commission v. National Securities, Inc.*, 393 U. S. 453, 468 (1969).

The enactment of Section 14(e) does not render unimportant for the future the questions involving Rule 10b-5 presented by this case. While it may no longer be necessary to rely on Rule 10b-5 in situations where complete relief is also available under Section 14(e), Rule 10b-5 retains its importance in areas not covered by that section. Thus by way of example, if a plaintiff were prevented from purchasing securities as a result of deception which was practiced upon others for the purpose of preventing them from selling to the plaintiff, but not incident to any tender offer, Section 14(e) would not apply. It would accordingly be important to the plaintiff that relief be available under Rule 10b-5. Moreover, the courts are using the interpretations placed upon Section 10(b) and Rule 10b-5 to interpret the meaning of Section 14(e). See, *e.g., Neuman v. Electronic Specialty Co.*, ____ F. Supp ____ CCH Fed. Sec. L. Rep. ¶ 92, 591 (N. D. Ill. 1969).[10]

The Commission shares our view on this point. See pp. 23-26 of the Commission's amicus brief filed in support of the petitioner's position on the appeal below.

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[10] The issue of standing may well be presented to this court by petitions from recent decisions of various Circuits where the new enactment is not applicable, *i.e., Crane v. Westinghouse Air Brake Co.*, 419 F. 2d 787 (2d Cir. 1969), *reh. denied*, March 4, 1970; *Kahan v. Rosenstiel*, ____ F. 2d ____, CCH Fed. Sec. L. Rep. ¶ 92,589 (3d Cir. Feb. 20, 1970); *Rekant v. Desser*, ___ F. 2d ___, CCH Fed. Sec. L. Rep. ¶ ____ Docket No. 25872 (5th Cir. Apr. 20, 1970); *City National Bank v. Vanderboom*, ____ F. 2d ____, CCH Fed. Sec. L. Rep. ¶ 92,587 (8th Cir. Feb. 20, 1970).

CONCLUSION

The application of the purchaser-seller limitation to deny standing to an investor who suffers damage because it is defrauded in violation of Section 10(b) and Rule 10b-5, in connection with a transaction which involves the purchase or sale of securities, is erroneous. Iroquois' relationship to the transaction in question and to the fraud which prevented its consummation—both as an actual purchaser of 9,000 shares and as an aborted purchaser of 41,000 shares—is more directly "in connection with a purchase or sale" than is that of a potential or hypothetical seller who may be forced by the antitrust laws or other considerations to become a seller of the securities at some time in the future.

For the foregoing reasons, the petition for a writ of certiorari should be granted and the decision below should be reversed.

Respectfully submitted,

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May 5, 1970.

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APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

No. 428—September Term, 1968.
Argued April 21, 1969 Decided November 3, 1969
Docket No. 32984

IROQUOIS INDUSTRIES, INC.,
Plaintiff-Appellant,

v.

SYRACUSE CHINA CORPORATION, WILLIAM R. SALISBURY, FOSTER T. RHODES, MALCOLM E. KELLEY, JAMES SALISBURY PASS, ROBERT M. SALISBURY, HAROLD C. BROWN & CO., INC., HAROLD C. BROWN, C. HERBERT FEUCHTER, and TOWLE MANUFACTURING COMPANY,
Defendants-Appellees.

Before:

LUMBARD, *Chief Judge,*
ANDERSON, *Circuit Judge,* and WYATT, *District Judge.**

Appeal by plaintiff Iroquois Industries, Inc. from an order of the United States District Court for the Western District of New York, John O. Henderson, *District Judge,* dismissing the action for failure of the complaint to state a claim upon which relief can be granted.

Affirmed.

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* Of the Sourthern District of New York, sitting by designation.

WYATT, *District Judge:*

The principal question, an important one, raised by this appeal is the extent to which Section 10(b) of the Securities and Exchange Act of 1934 (15 U.S.C. § 78a and following; the "1934 Act") is applicable in tender offer situations. Closely related is a question as to the continuing vitality of the decision of this Court in *Birnbaum* v. *Newport Steel Corp.*, 193 F.2d 461 (2d Cir.), cert. denied 343 U.S. 956 (1952).

The rule laid down in *Birnbaum* is that a civil action under Section 10(b) of the 1934 Act (15 U.S.C. § 78j(b)) may be maintained only by a purchaser or seller of securities. We find no reason to deviate from that rule in the present case. The decision below is therefore affirmed.

Iroquois Industries Inc. (Iroquois), the appellant, wanted to buy 50,000 shares of common stock of Syracuse China Corporation (Syracuse China), evidently to secure working control of Syracuse China. Iroquois made a public offer to purchase the shares and invited stockholders to tender their shares for purchase. The management of Syracuse China resisted the tender offer and it failed. Iroquois then brought this action, charging violations of Section 10(b) and other sections of the 1934 Act.

Judge Henderson in the Western District of New York granted motions of the defendants and, with an unreported memorandum opinion, dismissed the action as to all defendants for failure of the complaint to state a claim upon which relief can be granted (Fed. R. Civ. P. 12(b)(6)). We agree that the action should be dismissed.

The complaint has five counts, each purporting to state a separate claim. The averments of the complaint for present purposes must be assumed to be true.

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Jurisdiction of the first three claims is rested on Section 27 of the 1934 Act (15 U.S.C. § 78aa); there is no diversity jurisdiction of such claims. The fourth claim is against defendant Towle Manufacturing Company (Towle) only; there appears to be diversity jurisdiction as to this claim. The fifth claim is said to be within the pendent jurisdiction principle, *Hurn* v. *Oursler*, 289 U.S. 238 (1933).

The First Count

The first count avers the basic factual pattern applicable to all counts.

Plaintiff Iroquois is a Delaware corporation with its principal place of business in Buffalo.

Syracuse China is a New York corporation doing business in Syracuse. Syracuse China has outstanding 113,000 shares of common stock; there are some 600 stockholders. The individual defendants, except Brown and Feuchter, are officers or directors or both of Syracuse China. Defendant Harold C. Brown & Co., Inc. (Brown Inc.) is an investment banking house in Buffalo. The individual defendants Brown and Feuchter are connected with Brown Inc. Defendant Towle is a Massachusetts corporation which also does business in New York City.

Iroquois invited stockholders of Syracuse China to tender their shares for purchase and Iroquois agreed to purchase all shares tendered, up to 50,000 shares.

The defendants conspired together to prevent Iroquois from obtaining shares under the tender offer and did prevent Iroquois from obtaining shares. The defendants retained professional solicitors, at the expense of Syracuse China, who persuaded stockholders not to tender their shares. The defendants themselves asked stockholders not

to tender. Letters were written by defendants to the stockholders, falsely stating that Syracuse China was negotiating a merger, that negotiations for a merger with Towle were continuing, and that details of the merger would shortly be submitted; in fact, there was never any intention to conclude any merger with Towle but the talk was to mislead and to interfere with the tender offer. The letters of Syracuse China were false and misleading. The defendants advised stockholders that members of management would buy their shares if any stockholder wanted to sell; in fact, members of management did purchase a substantial number of shares. Towle aided the other defendants by conducting sham merger negotiations, knowing that no merger was intended. Brown Inc. and its officers and employees refused to advise the customers of Brown Inc. of the tender offer of Iroquois but instead advised them to sell their shares to members of the management of Syracuse China.

The claim in this count is that the acts of defendants were in violation of Section 10(b) of the 1934 Act and of Rule 10b-5 of the Securities and Exchange Commission (the "Commission") thereunder. The cited statute and Rule make it unlawful to employ fraud "in connection with the purchase or sale of any security."

We may put to one side most of the averments of the first count. The wrongful use of the funds of Syracuse China to defeat the tender offer might give rise to a derivative action in equity to recover for Syracuse China the amount of those funds. This, however, is not such an action and if it were, there would be no jurisdiction to entertain it because there is no diversity of citizenship.

There remain averments which are appropriate to a Section 10(b) claim, namely, that there were untrue statements

of material facts by defendants to stockholders of Syracuse China.

The history of Rule 10b-5 has been set out in the *Birnbaum* opinion. A summary will suffice here.

The Securities Act of 1933 (15 U.S.C. § 77a and following; the "1933 Act") contained a provision (Section 17(a); 15 U.S.C. § 77q) making it unlawful to employ fraud (including half-truths) "in the offer or sale of any securities." This applied only to fraud on *purchasers* of securities.

The 1934 Act contained a broader provision, Section 10(b), conferring rule making power on the Commission in respect to fraud "in connection with the *purchase* or *sale* of any securities . . ." (emphasis supplied). The rule making power thus included fraud on *sellers* of securities.

No rule was adopted for some years and as long as there was no rule, fraud on a purchaser was actionable under the 1933 Act but fraud on a seller was not actionable under either the 1933 Act or 1934 Act.

The Commission in May 1942 acted to close this loophole by adopting Rule 10b-5. This rule makes it unlawful to employ fraud (including half-truths) "in connection with the *purchase* or *sale* of any security . . ." (emphasis supplied), thus making it unlawful to employ fraud on *sellers* of securities as well as on purchasers.

In the light of this history, this Court decided in *Birnbaum* that Congress meant Section 10(b) to be "directed solely at that type of misrepresentation or fraudulent practice usually associated with the sale or purchase of securities" and that Rule 10b-5 "extended protection only to the defrauded purchaser or seller" (193 F.2d at 464). Professor Loss in 1961 gave his approval to this view as "basically correct" (3 Loss, Securities Regulation (here-

after "Loss") (2d ed. 1961) 1469) and has not since changed his mind (6 Loss (Supp. 1969) 3617).

In *Birnbaum*, plaintiffs were minority stockholders of Newport Steel Corporation (Newport). Their complaint showed the following situation. Feldmann owned enough stock of Newport to have voting control and was an officer and director of Newport. Follansbee Steel Corporation and Newport were negotiating for a merger which would have been highly profitable for stockholders of Newport. Feldmann rejected the merger and instead sold all his stock to Wilport Company (Wilport) for twice its market value. Wilport had been formed by a group of manufacturers who, with control of Newport, could secure its steel during a then critical shortage; this explained the premium paid. In letters which the defendants sent to stockholders of Newport both before and after the sale by Feldmann, there were misrepresentations and half-truths said to be in violation of Rule 10b-5. This Court held that, because the plaintiffs had not been either purchasers or sellers of Newport stock, they were not within the protection of Section 10(b) and that the complaint failed to state a claim. Dismissal of the action was affirmed.

Iroquois is not here complaining that it was misled by the acts of defendants as to any purchases or sales by it of Syracuse China stock; indeed, its basic complaint is that, because of the acts of defendants, it could not purchase such shares. In effect, Iroquois complains of fraud by defendants on the stockholders of Syracuse China who sold to the management of Syracuse China or otherwise refused to tender to Iroquois.

Appellant Iroquois and the Commission (as a friend of the Court) in substance invite us to overrule *Birnbaum;* they assert that its reasoning has already been weakened

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by several decisions of this Court. We do not so read the decisions and we do not believe that "the purchaser-seller limitation" of *Birnbaum* "has been relaxed" by later decisions of this Court, as the Commission contends.

In *Vine v. Beneficial Finance Co.*, 374 F. 2d 627 (2d Cir.), cert. denied, 389 U.S. 970 (1967), plaintiff owned shares in corporation A. Corporation B wanted to secure enough stock of A so that A and B could be merged. B made an offer to buy the stock of A and by fraudulent representations obtained 95% of such stock. Plaintiff did not tender his stock to B. A and B were then merged. This merger caused A (and its shares) to cease to exist. Plaintiff as to his A shares had only two alternatives: either to secure the fair value of those shares by judicial appraisal or to secure such value from B by agreement. An action under Section 10(b) was held to lie because by deceiving the other A stockholders, B forced plaintiff to become in substance a seller. It was expressly held that plaintiff was thus a "seller under the Act" and that defendant B was "a purchaser of plaintiff's stock" (374 F.2d at 635). The Court found it "unnecessary" to consider an "interesting contention" of the Commission that a plaintiff in a Section 10(b) action need not be either a purchaser or a seller.

Again in *A. T. Brod & Co. v. Perlow*, 375 F.2d 393 (2d Cir. 1967), a customer of a broker by fraud caused the broker to purchase securities from third persons. It was held that the broker was a "purchaser of the securities" (375 F.2d at 397) and that as such it could sue its customers who had placed fraudulent orders for stock. The Court also noted that a criticism by the Commission of the interpretation in *Birnbaum* as "too narrow" would not be considered because the broker "is clearly a purchaser of securities" (375 F. 2d at 397, fn. 3).

In these two cases, *Vine* and *Brod*, plaintiff was found to be a "seller" or a "purchaser" of shares; the fraud alleged was in connection with such sale or purchase. The two cases thus show no retreat from the proposition that a claim under Section 10(b) must relate to a purchase or sale as to which plaintiff was defrauded. We are unable therefore, to accept the conclusion that the two cases "seriously challenge, if not overrule, [the decision] in Birnbaum . . . ." *Entel* v. *Allen*, 270 F. Supp. 60, 69 (S.D.N.Y. 1967). The two cases do show that for a claim under Rule 10b-5 the purchase or the sale need not be between plaintiff and defendant, that there need not be "privity" between plaintiff and defendant. 3 Loss 1767-1771. This had been implicit, however, in the first decision of this Court that a violation of Rule 10b-5 gave rise to civil liability. There, purchasers of *common* stock on the market (not from defendants) were held to have a claim under Rule 10b-5 against the corporation, an underwriter and others based on fraud in a prospectus and registration statement for *preferred* stock. *Fischman* v. *Raytheon Mfg. Co.*, 188 F.2d 783 (2d Cir. 1951). After a somewhat confusing decision, *Joseph* v. *Farnsworth Radio & Television Corp.*, 198 F.2d 883 (2d Cir. 1952) (dissenting opinion by Frank, *J.*), it has become clear by now, attested by *Vine* and *Brod* (among other decisions), that liability under Rule 10b-5 does not depend on a securities transaction between plaintiff and defendant. 3 Loss (2d ed. 1961) 1767-1771, 6 Loss (Supp. 1969) 3890-3897. This has nothing whatever to do with the *Birnbaum* rule, that liability under Rule 10b-5 does depend on a purchase or a sale by plaintiff, as to which purchase or sale there is a claim of fraud.

In *Mutual Shares Corp.* v. *Genesco, Inc.*, 384 F.2d 540 (2d Cir. 1967), Genesco had made tender offers for stock

of Kress in the period July-October 1963. As a result of these tender offers and of a purchase of a large block of stock, Genesco obtained about 94% of the Kress stock. Beginning November 15, 1963 plaintiff *bought* shares of Kress. Plaintiffs commenced their action in November 1966. Their claim under Section 10(b) was (1) that there was fraud by Genesco in its offers to purchase the stock of Kress and (2) that after obtaining control of Kress in October 1963 Genesco manipulated the market price of Kress stock by keeping Kress dividends low so that Genesco could buy more Kress stock at depressed prices. Plaintiffs sought damages and an injunction against continuance of the manipulative scheme. It was held that plaintiffs had no claim for damages under Section 10(b) because no tender offers were made to them and they did not sell Kress stock to Genesco or to anyone else; they bought Kress stock. Plaintiffs, however, were held entitled to injunctive relief against the scheme to manipulate the market price of Kress stock; they were permitted thus to aid in the enforcement of the 1934 Act.

The decision in *Greenstein* v. *Paul*, 400 F.2d 580 (2d Cir. 1968), only about a year ago, followed *Birnbaum* as "still the rule" in this Circuit "at least insofar as actions for damages are concerned" (400 F.2d at 581). Plaintiff was the owner of stock of Corporation A. Eighty per cent of the stock of A was owned by Corporation B. The complaint charged a violation of Rule 10b-5 in that defendants, officers and directors of both A and B, had conspired to divert the assets of A to B, depressing the market price of the stock of A and enabling defendants to purchase at depressed prices the shares of A owned by the minority group. Plaintiff, however, had not sold his shares of A. Dismissal of the complaint was affirmed on the strength of the *Birnbaum* rule. The Court said:

> "It has long been the rule in this circuit that to maintain an action under § 10(b) of the Act and Rule 10b-5 of the Securities and Exchange Commission the plaintiff must have been a seller of the stock involved. Birnbaum v. Newport Steel Corp., 193 F.2d 461 (C.A. 2, 1952), cert. denied 343 U.S. 956, 72 S. Ct. 1051, 96 L. Ed. 1356 (1952). Although criticized, Entel v. Allen, 270 F. Supp. 60, 70 (S.D.N.Y., 1967), it still the rule at least insofar as actions for damages are concerned."

The *Birnbaum* rule recognizes the policy of Congress in enacting Section 10(b) and of the Commission in adopting Rule 10b-5, namely, the protection of defrauded purchasers and sellers. It is not the province of the courts to extend Section 10(b) to apply to transactions not intended to be covered by Congress. We do well to heed the words of Mr. Justice Black, writing for the Court in a case about another section of the 1934 Act, *Blau v. Lehman*, 368 U.S. 403, 413 (1962):

> "Congress can and might amend [the Act] if the Commission would present to it the policy arguments it has presented to us, but we think that Congress is the proper agency to change an interpretation of the Act unbroken since its passage, if the change is to be made."

That the conduct averred in any given case may be reprehensible does not mean that a federal remedy must be furnished by judges. The remedy in many cases may be found in the state courts which in New York, at least, afford redress as a "*prima facie* tort" for any wilful harm to the plaintiff. *Advance Music Corp. v. American Tobacco Co.*, 269 N.Y. 79, 84, 70 N.E.2d 401, 403 (1946). As

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Judge Anderson has recently said: ". . . all rights existing under State law are not also federal rights carrying a federal remedy." *Church* v. *Hegstrom*, ____ F.2d ____ (2d Cir., October 9, 1969) slip opinions 53, 56. If there is to be a federal remedy, it is the Congress which must create it. Indeed in the very area of the case at bar, tender offers, Congress last year adopted, effectve July 29, 1968, amendments (sometimes called the "Williams Bill") to add provisions in respect of tender offers to Sections 12, 13 and 14 of the 1934 Act. The amendments, among other things, added to Section 14 a new subdivision (e) reading as follows (15 U.S.C. §78n(e)):

> "It shall be unlawful for any person to make any untrue statement of a material fact or omit to state any material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading, or to engage in any fraudulent, deceptive, or manipulative acts or practices, in connection with any tender offer or request or invitation for tenders, or any solicitation of security holders in opposition to or in favor of any such offer, request, or invitation."

There was an informative House Report on the bill amending Section 14 of the 1934 Act (H.R. Rep. No. 1711, 90th Cong. 2d Sess. (1968); 1968 U.S. Code Cong. and Adm. News, pp. 2811-2823). This Report noted that tender offers had become an increasingly favored method for taking over control of publicly held corporations; that, because then existing laws had no disclosure requirements for tender offers, stockholders of the target corporation often did not have adequate information to decide whether to tender their shares or not; that this contrasted with

disclosure requirements applicable to exchange offers and to proxy fights; that the management of the target corporation, in resisting the tender offer, might repurchase for the corporation its own shares; and that then existing law contained no disclosure requirements in connection with such repurchases. The Williams Bill was reported favorably in order that, by its amendments to the 1934 Act, gaps in the securities law could be corrected.

That Congress enacted the new Section 14(e) to prohibit fraud by "any person" in respect of tender offers is at least an indication that in tender offer contests such as that at bar there was no standing to sue under Rule 10b-5 by either the tender offeror or by the target corporation. Judge Friendly has recently referred to new Section 14(e) as follows (*Electronic Specialty Co.* v. *International Controls Corp.*, 409 F.2d 937, 940 (2d Cir. 1969; emphasis supplied)):

> "In effect this applies Rule 10b-5 both to the offeror and to the opposition—very likely, *except perhaps for any bearing it may have on the issue of standing*, only a codification of existing case law."

And Judge Feinberg noted the introduction in Congress of the tender offer legislation with these words (*Mutual Shares Corp.* v. *Genesco, Inc.*, above cited, at 544):

> "Use of a tender offer by an outsider to obtain control of a publicly-held corporation is a fairly recent development. This means of corporate takeover has become increasingly popular, and has led to demands for legislative regulation to prevent abuses. Bills have been introduced in Congress designed to achieve this end. While not conclusive, this legislative activity at least indicates the conviction of many that existing

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statutes do not adequately cover the field. Indeed, the chairman of the Commission has stated, albeit not in his official capacity, that 'the bills now pending before Congress would fill a hiatus.'"

We adhere to the result and the reasoning of *Birnbaum*. Dismissal of the first count was proper.

The Second Count

This count against all defendants is based on the same averments as the first count but charges a violation of Section 14(a) of the 1934 Act (15 U.S.C. §78n(a)). There are no averments, however, that any defendant solicited "any proxy or consent or authorization in respect of any security." Judge Henderson was clearly right in dismissing this second count.

The Third Count

This count is directed only against defendants Brown Inc., Brown and Feuchter. The averments are the same as in the first count but the charge is a violation of Section 15(b)(4) (15 U.S.C. § 78o(b)(4)) and Section 15(c)(1) (15 U.S.C. § 78o(c)(1)) of the 1934 Act.

Section 15(b)(4) is directed to conduct of a registered broker or dealer. Brown Inc., Brown and Feuchter are averred to be such. Section 15(b)(4) makes Section 10(b) applicable to registered brokers and dealers, whether the mails or instrumentalities of interstate commerce are used or not. Section 15(c)(1) prohibits fraud by a registered broker or dealer in any use of the mails or instrumentalities of interstate commerce to induce the purchase or sale of any security.

Dismissal of the first count requires for the same reasons that the third count be dismissed.

THE FOURTH COUNT

This count against defendant Towle only is based on the same averments as the first count but relies on diversity jurisdiction.

The charge against Towle is that it "aided and abetted the other defendants." If, as we have found, no claim is stated against "the other defendants," then plainly no claim is stated against the aider and abetter and dismissal of the fourth count was proper.

THE FIFTH COUNT

This count against all defendants is based on state law and rests on the principle of pendent jurisdiction. *Hurn* v. *Oursler*, 289 U.S. 238 (1933).

We have found that the federal claims must be dismissed. The Supreme Court in such a situation has instructed (*United Mine Workers of America* v. *Gibbs*, 383 U.S. 715, 726 (1966)):

> "Certainly, if the federal claims are dismissed before trial, even though not insubstantial in a jurisdictional sense, the state claims should be dismissed as well."

Dismissal of the fifth claim was therefore proper.

The order appealed from is affirmed. We do not reach the point pressed by certain appellees that summary judgment should have been directed for defendants on the facts said to have been undisputed.

APPENDIX B

UNITED STATES DISTRICT COURT

WESTERN DISTRICT OF NEW YORK

IROQUOIS INDUSTRIES, INC.,

Plaintiff,

vs.

SYRACUSE CHINA CORPORATION, WILLIAM R. SALISBURY, FOSTER T. RHODES, MALCOLM E. KELLEY, JAMES SALISBURY PASS, ROBERT M. SALISBURY, HAROLD C. BROWN & CO., INC., HAROLD C. BROWN, C. HERBERT FEUCHTER, and TOWLE MANUFACTURING COMPANY,

Defendants.

Civil 1967-310.

This action was commenced by the plaintiff, Iroquois Industries, Inc., following its unsuccessful bid to gain control of the defendant, Syracuse China Corporation, through the vehicle of a tender offer to stockholders. Before the court are motions to dismiss the plaintiff's complaint for lack of jurisdiction over the subject matter and for failure to state a claim for which relief can be granted, and motions for summary judgment.

In passing upon the defendants' motions to dismiss, the allegations of the complaint must be accepted as true. See *Vine v. Beneficial Finance Co.*, 374 F. 2d 627, 632-633 (2d Cir. 1967); *A. T. Brod Co. v. Perlow*, 375 F. 2d 393, 395 (2d Cir. 1967).

Initially, the complaint recites the fact that on June 12, 1967, Iroquois Industries, Inc. issued an invitation to shareholders of Syracuse China Corporation to tender their shares at sixty dollars per share. This price was substantially in excess of the then existing market price for such shares. Under the terms of this invitation, Iroquois Industries, Inc. was obligated to purchase 50,000 shares of Syracuse China Corporation stock if that number were tendered on or before June 30, 1967. Shares tendered in excess of the 50,000 shares sought could be purchased in whole or in part at Iroquois Industries, Inc.'s option on a first come, first served basis. On June 15, 1967, the tender offer was amended in part to bind Iroquois Industries, Inc. to the purchase of any and all shares tendered up to the 50,000 shares which were sought.

The complaint purports to state five causes of action. The first, against all defendants, is brought under section 10(b) of the Exchange Act (15 U. S. C. § 78j(b)) and Rule 10b-5 thereunder (17 C. F. R. § 240.10b-5). The second, again against all defendants, is brought under section 14(a) of the Exchange Act (15 U.S.C. § 78n(a)) and Regulation 14A thereunder (17 C. F. R. § 240.14a). The third, against defendants Harold C. Brown & Co., Inc., Harold C. Brown and C. Herbert Feuchter only, is brought under section 15(b)4 of the Exchange Act (15 U. S. C. § 78(b)(4)) and Regulation 15b4-8 thereunder (17 C. F. R. § 240.0-8), as well as section 15(c)(1) of the Exchange Act (15 U. S. C. § 78o(c)(1)) and Regulation 15c1 thereunder (17 C. F. R. § 240.15c1). The fourth, against the defendant Towle Manufacturing Company only, is based on this court's diversity jurisdiction (28 U. S. C. § 1332). The fifth, against all defendants, is based upon a claim of pendent jurisdiction.

Each of the claims alleges a conspiracy among the defendants and charges fraud, malice and wrongdoing to interfere with and thwart plaintiff's invitation to tender. Named as parties defendant are the Syracuse China Corporation and five of its officers and directors; Harold C. Brown & Co., Inc., a dealer in securities having local offices, its president and director and an executive employee; and Towle Manufacturing Company, a Massachusetts corporation.

A review of the basic allegations of the complaint in support of the claims of conspiracy and fraud serves to point up the issues presented. These allegations appear in subparagraphs (a) through (p) of paragraph 25 of plaintiff's first cause of action and are incorporated by reference in the remaining four causes of action.

Subparagraphs (a) through (d) merely allege that Syracuse China and the defendant officers and directors retained professional solicitors, at corporate expense, who successfully solicited shareholders to refrain from tendering shares. Although plaintiff alleges that this was done "illegally and wrongfully," in view of the requirements of Rule 9(b) of the Federal Rules of Civil Procedure, the court must assume the absence of fraud. No jurisdictional basis is present to support a stockholder's derivative suit.

Subparagraphs (e) (f) and (g) allege similar efforts, including use of interstate telegrams and the mails, to defeat plaintiff's tender offer by employees, agents and the president of Syracuse China Corporation.

Subparagraphs (h) (i) and (j) begin to strike at the heart of the issues raised by the motions to dismiss. It is claimed that, in an effort to dissuade them from tendering their shares, stockholders were advised by Syracuse China

and its president, through use of the mails, of negotiations looking toward a more favorable tax-free merger with another company which was identified as Towle Manufacturing Company. The plaintiff charges that the negotiations were sham and were designed to defeat the tender offer through misleading the shareholders of Syracuse China. Towle Manufacturing Company is alleged to have knowingly aided and abetted the aforementioned defendants in furtherance of the alleged scheme.

Subparagraphs (l) and (m) allege management's and its agents' and employees' efforts to purchase shares and of announcements of the Towle merger negotiations in connection with that effort. Subparagraph (m) apparently includes the Harold C. Brown & Co., Inc. defendants among those defendants allegedly impressing shareholders with the value of the Towle merger and advising the sale of stock to management rather than the plaintiff.

Subparagraph (n) again is a derivative action, claiming use of corporate funds in furtherance of the efforts to frustrate the tender offer.

Subparagraph (o) is directed against the defendants, Harold C. Brown & Co., Inc., its president, Harold C. Brown, and the executive employee C. Herbert Feuchter. It is claimed that these defendants (a) advised shareholders not to tender shares to the plaintiff, (b) instead urged shareholders to sell to management, (c) refused to advise the beneficial owners of the shares registered in the name of Harold C. Brown & Co., Inc. of the plaintiff's tender offer, and (d) refused to furnish to such beneficial owners copies of plaintiff's tender offer although copies were furnished to it and expenses for the same were tendered.

Subparagraph (p) alleges that defendant's communications to stockholders contained statements violative of Rule 10b-5.

The court first will consider the plaintiff's first cause of action under section 10(b) of the Act and Rule 10b-5.

Section 10(b) provides in pertinent part:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange . . .
>
> (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

Rule 10b-5 provides:

> It shall be unlawful for any person directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,
>
> (1) To employ any device, scheme, or artifice to defraud,
>
> (2) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

The opinion of the Second Circuit Court of Appeals, in *Mutual Shares Corp. v. Genesco, Inc.*, 384 F. 2d 540 (1967), includes an excellent and succinct review and analysis of the developing law governing civil liability for transactions in securities. The court, at pages 543-544, observed:

> Section 10(b) and Rule 10b-5 have been the focal point for a spectacular growth in the law governing civil liability for transactions in securities. This has been all the more remarkable because the Act does not explicitly provide a private civil remedy for violations of the section and Rule, and the Supreme Court has never held that one exists, although J. I. Case Co. v. Borak, 377 U. S. 426, 84 S. Ct. 1555, 12 L. Ed. 2d 423 (1964), impliedly suggests that it does. Nevertheless, it is now common ground that an injured investor does have a private cause of action under Rule 10b-5, *e.g.*, Fischman v. Raytheon Mfg. Co., 188 F. 2d 783 (2d Cir. 1951). However, various concepts have been utilized to limit liability under the sweeping language of the Rule, although none is specifically required by it. 3 L. Loss, Securities Regulation 1763-67 (2d ed. 1961). Thus, a requirement of privity was at first suggested [citing cases] but has more recently been ignored, *e.g.*, [citing cases]. However, the search for limiting doctrine has continued. Thus, some courts have looked to see whether a plaintiff actually relied on the allegedly fraudulent statement whether such reliance was reasonable, whether the fraud actually caused the harm to plaintiff, whether the plaintiff's injury was

foreseeable, and whether plaintiff falls within the category of a buyer or seller of securities.

With respect to tender offers in particular, the court, at page 544, noted:

> Use of a tender offer by an outsider to obtain control of a publicly-held corporation is a fairly recent development. This means of corporate takeover has become increasingly popular, and has led to demands for legislative regulation to prevent abuses. Bills have been introduced in Congress designed to achieve this end. While not conclusive, this legislative activity at least indicates the conviction of many that existing statutes do not adequately cover the field. Indeed, the chairman of the Commission has stated, albeit not in his official capacity, that "the bills now pending before Congress would fill a hiatus."

From a review of the cases in this area, it would seem apparent that the courts, in developing a limited doctrine, have not blindly applied any particular test in this complex field but have recognized the exigencies arising in a given case and thereby have reached results conforming to the purposes of the Act.[1]

In the present case the plaintiff, while a purchaser, cannot claim to be either a defrauded purchaser[2] or a purchaser who, in purchasing its shares, relied in any way upon the alleged fraud.[3] While *Moore v. Greatamerica*

[1] *Compare* Birnbaum v. Newport Steel Corp., 193 F. 2d 461 (2d Cir.), *cert. denied*, 343 U. S. 956 (1952) *with* A. T. Brod & Co. v. Perlow, 375 F. 2d 393, 397, n. 3 (2d Cir. 1967); *and* Vine v. Beneficial & Fin. Co., 374 F. 2d 627, 636 (2d Cir. 1967).

[2] See Birnbaum v. Newport Steel Corp., n. 1, *supra*.

[3] See List v. Fashion Park, Inc., 340 F. 2d 457, 462-463 (2d Cir.), *cert. denied*, 382 U. S. 811 (1965); Janigan v. Taylor, 344 F. 2d 781 (1st Cir. 1965).

Corp., 274 F. Supp. 490 (N. D. Ohio 1967) may be read as lending support to plaintiff's claim that it should be viewed as being entitled to relief, the numerous remaining cases, to which the court's attention has been directed, clearly are distinguishable and provide little or no support for that result.

That the maker of a tender offer may suffer damage by false statements emanating from management, particularly when it binds itself to the purchase of a large number of the shares tendered, may well be argued. Notwithstanding that possibility, this court has serious reservations as to whether section 10(b) relief may be viewed as extending to makers of tender offers.

As the previously quoted portion of the opinion in *Mutual Shares Corp. v. Genesco, Inc.*, *supra*, noted, the tender offer has become a popular tool for corporate takeovers. Generally speaking, nothing other than the identity of the offeror and the terms of the offer need be disclosed to shareholders. The offer, of necessity, usually includes a substantial premium over market value of the shares sought and, therefore, may be assumed to be attractive to the shareholders. Thus, while much may be at stake from the shareholders' point of view, he at this point may be forced to make a relatively uninformed judgment. Management's only defense then is to endeavor to convince shareholders that the offer, for one reason or another, should not be accepted. In so doing, this court would be prone to accept a view of exposure to civil liability under section 10(b) insofar as the shareholders solicited are concerned. Such a result would appear to promote the purposes of the Act. Extending similar relief to the maker of tender offers, however, would not appear to be within the ambit or the purposes of the Act and would

involve other or collateral considerations which fairly may not be expected to serve the salutory purposes of the Act.

Were a contrary result reached, practically any response by management, faced with a tender offer, immediately could be challenged in the courts. Attendant publicity, including charges and possibly counter-charges, resulting delay in dissemination of information, etc., all could serve to further worsen the individual shareholders' plight in reaching an informed decision. While the courts obviously would strive to avoid or diminish such consequences, the likelihood of real success in such an endeavor would appear dim. In short, absent regulatory supervision under a scheme established by comprehensive legislation, the result urged by plaintiff promises to worsen a situation already the subject of great concern.

While it is true that the courts have taken a permissive approach to complaints in this area, *Donlon Industries, Inc. v. Forte*, C. C. H. Fed. Sec. L. Rep. ¶ 92.196 (S. D. N. Y. 1968), for the reasons outlined above, the court concludes that the plaintiff's first cause of action must be viewed as failing to state a claim for which relief can be granted and is dismissed.[4]

As was previously mentioned, the second cause of action against all defendants purports to be brought under section 14(a) of the Exchange Act and Regulation 14A thereunder. The court fails to comprehend how the plaintiff's complaint may be viewed as stating a claim for un-

[4] After the submission of this case the Second Circuit Court of Appeals rendered its decision in Securities and Exchange Commission v. Texas Gulf Sulphur (Aug. 13, 1968 slip opinion p. 3587). The parties have expressed their views regarding that case and the court is of the opinion that the principles outlined in that decision, concerning the "in connection with" requirement of section 10(b), have no application to an action between private litigants on a tender offer situation such as this. See Greenstein v. Paul, *et al.* (Aug. 20, 1968 Second Circuit slip opinion p. 3403).

lawful proxy solicitation. Accordingly, the second cause of action also is dismissed.

The third cause of action is based upon somewhat similar rules to those discussed in connection with the first cause of action but which instead govern brokers in their relationship with their customers. This cause of action is directed against the defendants, Harold C. Brown & Co., Inc., Harold C. Brown and C. Herbert Feuchter. For reasons analogous to those previously discussed, this cause of action is dismissed.

With respect to the fourth cause of action based upon diversity jurisdiction and directed against Towle Manufacturing Company only, the court fails to find any basis for relief in the absence of the other parties and, accordingly, this cause of action is dismissed.

The fifth and final cause of action, relying upon pendent jurisdiction, must fail in light of this court's disposition of the first three causes of action and therefore is dismissed.

Submit order on five (5) days' notice.

/s/ JOHN O. HENDERSON,
United States District Judge.

Dated: September 23, 1968.